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C O N F I D E N T I A L SECTION 01 OF 02 HANOI 000052

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TAGS: [ECON](#) [ENRG](#) [EPET](#) [PBTS](#) [PREL](#) [VM](#)

SUBJECT: 2008 RECAP OF THE SINO-VIETNAM SOUTH CHINA SEA TERRITORIAL DISPUTE

REF: A. REF:

- [1B.](#) (A) HANOI 1094: DESPITE RESENTMENT
- [1C.](#) CHINA POLICY MARKED BY PRAGMATISM & CAUTION
- [1D.](#) (B) HANOI 1287: BP SEEKS TO TERMINATE LEASE
- [1E.](#) (C) HANOI 0579: BP TRANSFERS OPERATORSHIP TO PETROVIETNAM
- [1F.](#) (D) HANOI 1016: NORWEGIAN VESSEL SPOTTED NEAR DISPUTED BLOCK
- [1G.](#) (E) HANOI 1241: VIETNAM NEGOTIATES DEAL WITH GAZPROM

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Classified By: AMBASSADOR MICHAEL MICHALAK FOR REASONS 1.4 (B) AND (D)

[11.](#) (C) Summary: Despite final land border demarcation and progress settling the maritime boundary beyond the Gulf of Tonkin, 2008 ended without evident progress in the Sino-Vietnam territorial dispute in the South China Sea. In November, BP gave notice that it would seek to terminate its leases in Blocks 5-2 and 5-3, where BP was leading a planned \$2 billion project with ConocoPhillips (CoP) and Japan's Idemitsu. CoP subsequently informed PetroVietnam (PVN) that it too would divest its interest in the blocks. China has warned ExxonMobil (EM) about potential future activity in two sets of disputed blocks, but EM has signaled its plans to proceed. In 2007, Chevron suspended activity in Block 122 after warnings by China. Chevron has requested a contract extension from PVN but has not yet received a reply. Houston-based Plains Exploration and Production, formerly Pogo Producing Company, said recently that it has completed seismic work in disputed Block 124 and planned to drill during the upcoming 2009 season. End summary.

THE TYRANNY OF THE NINE DOTTED LINES

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[12.](#) (C) Despite agreement on the final demarcation of their land border and progress settling the maritime boundary beyond the Gulf of Tonkin (REF A), Vietnam and China made no evident progress in 2008 in resolving the offshore sovereignty dispute in the South China Sea (or "East Sea" as the Vietnamese term it). The offshore dispute continues to entangle multiple multinational energy companies, including U.S.-based ExxonMobil, Chevron, ConocoPhillips and Plains Exploration & Production. 2008 also produced the dispute's first major investment casualty, as BP notified PVN in November that it would seek to terminate its leases in Blocks 5-2 and 5-3 in the Nam Con Son Basin, where BP had been leading a planned \$2 billion integrated gas field and pipeline project with ConocoPhillips and Japan's Idemitsu (REF B).

BP, CONOCOPHILLIPS THROW IN THE TOWEL

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¶ 13. (C) In 2007, China warned BP that its activity in the blocks infringed Chinese sovereignty. The government of China did not directly threaten BP's expansive energy portfolio in China, but the implication was clear. The lease in 5-3 expired in December 2008 with the lease in 5-2 set to expire at the end of 2009, and there were questions whether the government of Vietnam (GVN) would renew the partnership given the ongoing delays and BP's significant economic interests in China. The protests by China led BP/CoP/Idemitsu to first suspend and then cancel the 2007 work season and transfer operatorship for the 2008 season to PetroVietnam to avoid missing critical deadlines (REF C). PetroVietnam proceeded to hire a Norwegian-flagged 3D/4D seismic vessel to carry out geophysical mapping and 3D seismic surveys during the Beijing Summer Olympics, which came and went without major new protests by China (REF D).

¶ 14. (C) A BP Vietnam official told us last week that multinational energy firms from Russia, Canada and Japan were interested in taking over the BP leases, but that PVN had thus far made little progress in securing a new operator for the blocks. The official speculated that Vietnam was leery about inviting new participation for fear of provoking China. BP, which will take a \$200 million loss on the project, has said its move is strictly a "commercial decision." Japanese Ambassador to Vietnam Sakaba recently told the Ambassador that Idemitsu would like to remain involved in the project but could not go it alone.

¶ 15. (C) ConocoPhillips held the right under its contract to either retain its 20 percent share or push for a majority stake in the blocks, including operatorship. The company,

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however, informed PVN in December 2008 that it too would divest its interest in the blocks. Nguyen Ba Hung, Director General of the GVN's Ministry of Foreign Affairs America's Department, subsequently complained to the DCM that CoP's action "sent a very bad signal all the way to the Prime Minister," given the PM's discussions with President Bush about the investment and trip to Houston in 2008 to visit CoP headquarters.

CHEVRON DEFERS PROJECT; EXXON AND PLAINS MOVE AHEAD

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¶ 16. (C) The dispute continues to thwart other U.S. investments as well. In August 2007, Chevron suspended exploration in Block 122 near Nansha Island, 250 kilometers east of the Vietnamese port of Qui Nhon, after the Chinese Embassy in Washington warned Chevron and its Malaysian partner Petronas to halt activity. A Chevron official told us last week that Chevron had no plans to conduct physical work in the block in 2009 or 2010. The official said Chevron has requested a contract extension from PVN to allow Chevron to fulfill its contractual commitments in 2011, but had not yet received a reply.

¶ 17. (C) China has also warned ExxonMobil about its planned activity in Blocks 117-8-9 (offshore Da Nang) and 156-9 (located due east of BP's former blocks). ExxonMobil has signaled that it plans to proceed and the company is currently negotiating with PetroVietnam to incorporate all seven blocks, all of which are still in the preliminary phase, under a general framework agreement. ExxonMobil had also been engaged in periodic discussions for more than a year with PVN to negotiate a deal for Blocks 129-132, before PVN unexpectedly awarded a 30-year operating lease to Russia's Gazprom in a direct bilateral deal on October 27, 2008 (REF E).

¶ 18. (C) Houston-based Plains Exploration & Production, formerly Pogo Producing Company, holds a concession in Block

124 offshore central Vietnam (south of Chevron's Block 122). In September 2007, the Chinese Consulate in Houston warned then-leaseholder Pogo to cease its exploration activity, although the company resumed work during the 2008 work season. Plains officials told us recently that the company has completed the seismic work required by its production sharing contract with PVN and would soon finish a site survey in preparation for drilling during the 2009 season.

¶ 9. (C) Soon after announcing the completion of their land border demarcation, Vietnam and China convened this month for the fifth round of talks to discuss cooperation, demarcation and mutual development in the Tonkin Gulf. Related discussions to resolve the South China Sea dispute, however, remain elusive. In August 2008, then-BP Vietnam General Director Gretchen Watkins complained to the Ambassador that state-run Chinese oil company CNOOC and PVN refused to discuss the offshore disagreement during the two companies' regular commercial talks, and appeared to want BP to mediate or craft a commercial resolution to the dispute, a role that BP was unwilling to play. Japanese Ambassador Sakaba told the Ambassador that he has encouraged the GVN to negotiate with China via ASEAN, but that related offshore territorial conflicts between China and other ASEAN member states were hindering the ability of the group to work together on the issue. We have similarly urged Vietnam to better use ASEAN to increase its leverage with China; however, GVN officials bluntly concede that ASEAN's consensus-driven decision-making process renders a firmer collective response all but impossible.

MICHALAK